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Key Provisions of CPUC-PG&E Proposed Settlement

The proposed settlement agreement between the California Public Utilities Commission (CPUC) staff, and Pacific Gas and Electric Company and its parent PG&E Corporation, would resolve the competing plans of reorganization in the utility's Chapter 11 proceeding and end litigation between PG&E and the CPUC relating to the energy crisis. The proposed settlement agreement would become effective after extensive public hearings and review and approval by the CPUC and after review and approval by the boards of directors of both the utility and PG&E Corporation. It also must be incorporated into a new plan of reorganization to be submitted to the Bankruptcy Court for its approval.

Under the provisions of the proposed settlement agreement, it is expected that the utility would emerge from Chapter 11 protection in early 2004 as a vertically integrated utility, subject to the traditional ratemaking jurisdiction of the CPUC. Just as importantly, it is expected that the utility would be an investment grade company, capable of fulfilling its obligations to serve its customers and operating safely and reliably on a sound financial basis going forward. In order to achieve these goals, the proposed settlement agreement provides the following:

Ratepayer Protections

- The CPUC staff projects that rates would come down starting January 1, 2004, by approximately \$350 million per year. This means that average retail electric rates are projected to come down by about half a cent (from their current 13.87 cents/kwh) on January 1, 2004, and continue falling to about 12.8 cents by 2008.
- The CPUC would retain control over setting retail electric rates for customers of Pacific Gas and Electric Company under California law.
- Ratepayers would directly benefit from any refunds, claim offsets or other credits from generators or other energy suppliers relating to the utility's power procurement costs.

Regulatory Stability

- The utility would remain a vertically integrated utility subject to CPUC regulation, just as it is today.
- As part of the proposed settlement, PG&E and the CPUC would resolve all significant ratemaking and regulatory litigation that arose between them as a result of the energy crisis. The proposal would provide the opportunity to rebuild the respect and trust between PG&E and the CPUC that had been damaged as a result of the energy crisis.
- The CPUC would commit to provide timely review and decisions in the future on the utility's ratemaking requests, including timely action on recovery of costs associated with electric and gas distribution, utility-retained generation, gas commodity

procurement, existing QF contract costs, the new regulatory asset, and any new, reasonable investment in utility plant and assets.

- Future power procurement issues would be reviewed by the CPUC consistent with the provisions of Assembly Bill 57, signed into law in 2002, which calls for stable and prudent regulatory guidelines up front for utility power procurement decisions.
- To integrate further the future power procurement plans of the utility with existing power supply contracts entered into by the State during the energy crisis, the utility would agree to take over responsibility for the DWR power supply contracts, provided that it has been determined that the utility can maintain a sufficiently strong credit rating (no less than “A” from Standard and Poor’s and “A2” from Moody’s) when assuming the contracts, and that the CPUC finds that the contracts are just and reasonable and ensures all contract costs are recoverable on a timely basis. The CPUC would retain discretion to review the prudence of PG&E’s administration and dispatch of the DWR contracts consistent with applicable law.
- The CPUC would establish a regulatory asset as a separate part of the utility’s rate base. The \$2.21 billion regulatory asset would be recovered in retail electric rates over nine years beginning January 1, 2004, and would be subject to reduction to reflect refunds, claim offsets or other credits from generators or other energy suppliers.

Environmental Protections

- The utility would provide conservation easements or fee interests in approximately 140,000 acres of watershed and other lands around its hydroelectric generation facilities and the Carizzo Plains to public agencies or non-profit resource conservation organizations. The donated lands have been estimated to be worth \$300 million.
- The utility would establish a non-profit corporation to oversee the lands and the environmental enhancements, and fund the corporation with \$70 million over a 10-year period through electric rates.
- The utility would create a new non-profit corporation dedicated to support research and investment in clean energy technology, primarily in the utility’s service area. The utility’s shareholders would contribute \$15 million over five years to fund this project.

Treatment of Creditors

- All of the utility’s existing creditors would be paid in cash under the proposed settlement plan, except for certain pollution control bonds, which, along with the utility’s preferred stock, would be reinstated.

Treatment of Shareholders

- PG&E Corporation and utility shareholders would forego dividend payments (which have been suspended since January 2001) until July 1, 2004 – a total of

approximately \$1.7 billion. After July 1, 2004, there would be no further extraordinary restrictions on the ability of PG&E Corp. or the utility to pay dividends on a going-forward basis.

Dismissal of Filed Rate Case, Other Litigation and Proceedings

- On or after the effective date of the settlement plan, the utility would dismiss with prejudice its pending federal lawsuit against the CPUC to recover its previously incurred costs of providing electric service from ratepayers under the federal filed rate doctrine. The utility would also withdraw its current plan of reorganization.
- On or after the effective date of the settlement plan, the utility and the CPUC would execute full mutual releases and dismissals with prejudice of all significant claims, actions and regulatory proceedings arising out of or related in any way to the energy crisis or the implementation of AB 1890.
- Pending approval of the proposed settlement agreement and emergence from Chapter 11, the utility will request a stay of all actions before the Federal Energy Regulatory Commission (FERC), the Nuclear Regulatory Commission (NRC), the Securities and Exchange Commission (SEC) initiated to implement the utility's plan of reorganization. In addition, the utility will suspend all actions to obtain or transfer licenses, permits and franchises to implement the utility plan. Assuming the proposed settlement and new plan of reorganization are approved, the utility would withdraw all such applications for regulatory approvals, licenses, permits and franchises associated with the current utility reorganization plan.
- The CPUC, the utility and PG&E Corp. would agree to the jurisdiction of the Bankruptcy Court in order to implement the proposed settlement and new plan of reorganization, and to resolve any disputes or disagreements that may arise during the term of the settlement. The CPUC would agree to waive all existing and future claims of sovereign immunity, and all other similar immunities, as a defense in connection with any action concerning the enforcement of the proposed settlement.
- The settlement agreement would terminate in nine years.

Next Steps/Approvals

- The proposed settlement will be subject to extensive public review and hearings before the CPUC, and a vote of the CPUC. The proposal also is subject to the approval of the boards of directors of PG&E Corporation and the utility. If all such approvals have not been received by December 31, 2003, any party may terminate the proposed settlement agreement.
- The proposed settlement plan will be subject to a vote by creditors and approval by the Bankruptcy Court.
- The settlement plan will not become effective until (1) Standard & Poor's and Moody's have issued investment-grade credit ratings for the utility and the securities to be issued under the plan, and (2) the CPUC has given final approval for all rates, tariffs, and agreements necessary to implement the plan.